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IN THE

Supreme Court of the United States

OCTOBER TERM, 1952

NO. 231

MARK McGEE, R. H. RUCKER, KATE H. PEARCE AND CHARLES P. ATKINSON,

Petitioners

VS.

RECONSTRUCTION FINANCE CORPORATION AND MERCANTILE NATIONAL BANK AT DALLAS, INTERVENOR,

Respondents

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT AND BRIEF IN SUPPORT THEREOF

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VS.

RECONSTRUCTION FINANCE CORPORATION AND MERCANTILE NATIONAL BANK AT DALLAS, INTERVENOR,

Respondents

PETITION FOR WRIT OF CERTIORARI

To the Honorable The Supreme Court of the United States:

Mrs. Kate H. Pearce and Charles P. Atkinson pray that a writ of certiorari issue to review the judgment entered in this case by the United States Court of Appeals for the Fifth Circuit.

Opinions Below

The opinion of the Court of Appeals is reported in *McGee et al., v. Reconstruction Finance Corp. et al.*, 195 F. 2d 396. The District Court's oral opinion is in the record at pages 249, 250, 251.

Summary Statement of Matter Involved

This Court of Appeals summarized the matter involved in the following language:

> "The trial had in the Court below was initiated by the filing of a complaint by Reconstruction Finance Corporation, for and on behalf of itself and Mercantile National Bank of Dallas, seeking to foreclose liens against certain equipment and securities alleged to have been pledged as collateral to secure a loan in the original amount of $230,000. The loan was evidenced by a note dated March 26, 1946, payable to Mercantile National Bank and signed by C. M. Pearce, individually and as President of Apex Drilling Company, Inc. The note was alleged to have been transferred and assigned to Reconstruction Finance Corporation, together with all liens securing the payment thereof, with reservation that under a participation agreement existing between the payee and Reconstruction Finance Corporation the former held an equitable interest of 25% in the note and collateral and in any and all proceeds received therefrom.
>
> "In addition to other described collateral expressly pledged to secure the payment of the note, the complaint alleged that certain 'separate collateral' agreements and the collateral covered by them were subject to foreclosure to satisfy the unpaid balance of the note, and named as defendants the parties who claimed an interest in the collateral covered by the agreements."

The collateral referred to as expressly pledged to secure the $230,000.00 note was described in a chattel mortgage. (R. 284-302) The twenty-five shares of capital stock of the Travelers Insurance Company, the property of Kate H. Pearce, and the ten shares of capital stock of the Travelers Insurance Company, the property of Charles P. Atkinson, is the property of

petitioners covered by the above mentioned "separate collateral agreements," and is the subject of this petition for certiorari.

> ". . . Kate H. Pearce and Charles P. Atkinson answered admitting that their stock was pledged to the Bank under collateral agreements to secure the personal indebtedness of C. M. Pearce, but denying that it was subject to the liability upon which foreclosure was sought. . . .
>
> "Trial was had by the Court without a jury. At the commencement of the trial the Mercantile National Bank was allowed to intervene as a party plaintiff and to adopt the pleadings of Reconstruction Finance Corporation. At the close of the evidence the trial Court found the facts as announced in an oral opinion and entered judgment for the complainants that the securities originally pledged to the Bank as collateral were subject to their claim. C. M. Pearce and Apex Drilling Company, Inc. have not appealed. The remaining defendants have prosecuted this appeal from the judgment as it affects their respective claims to the securities.
>
> "The provisions of the 'separate collateral agreements' here involved furnished the foundation for appellees' claim of lien. One of these, dated May 21st, 1945, was executed by Kate H. Pearce and pledged 25 shares of the capital stock of Travelers Insurance Company to secure the payment of all indebtedness 'now owing' to the Bank 'or which may hereafter become owing to it' by Kate H. Pearce and C. M. Pearce. The other separate collateral agreement, dated June 7th, 1945, was executed by C. M. Pearce, Jean E. Collins and Charles P. Atkinson and, as it existed at the time of suit, pledged 20 shares of the capital stock of Travelers Insurance Company, 20 shares of Union Bank & Trust Company stock and the cashier's check referred to above, for the purpose

of securing the Bank in the payment of all indebtedness then owing to it or which might thereafter become owing to it by these signatories or either of them. Each collateral agreement provided that the property pledged 'may be held by said Bank as security for any and all debts and obligations . . . to said Bank for the payment of money, whether such debts, liabilities and obligations now exist, or are hereafter incurred or arise, and whether the obligation or liability . . . be direct, contingent, primary, secondary, joint, several, joint and several, or otherwise, and whether such obligations be of the same character or different,' and all rights and powers thereunder, 'together with all securities then held in pledge hereunder, may be transferred and assigned by said Bank at such times and upon such terms as it may deem advisable; and such assignee shall succeed to all rights and powers of said Bank hereunder.'

"It appears from the evidence that C. M. Pearce secured several loans from Mercantile National Bank during the period from May 2nd, 1945 to June 8th, 1948. On September 15th, 1945, he borrowed $200,000 from the Bank on a note signed by C. M. Pearce, d/b/a Apex Drilling Company. On or about March 26th, 1946, Apex Drilling Company was incorporated and on that date the corporation, and C. M. Pearce individually, secured a loan from the Bank in the amount of $230,000, the proceeds of which were used to satisfy the $200,000 note and other debts of Pearce, d/b/a Apex Drilling Company. The payment of this note was specifically secured by a chattel mortgage covering the assets of the new corporation and by an assignment of all of the stock of that corporation.[1]

---

[1]"This note defined indebtedness as 'The term "the Indebtedness" as used herein shall mean the indebtedness evidenced by this Note and any and all other indebtedness of the undersigned as Payee, * * * The term "the Collateral" as used in

On February 5th, 1947, the $230,000 note, together with the chattel mortgage, was assigned by the Bank to Reconstruction Finance Corporation without recourse. On February 13th, 1947, Reconstruction Finance Corporation issued a 'certificate of interest' certifying that the Bank retained an interest of 25% of the loan. The transactions between Reconstruction Finance Corporation and the Bank were effected in accordance with "a participation agreement," dated April 14th, 1945, which contained provisions as to sharing of collateral.[2]

"At all times, from the date of their execution until the time of trial, the Bank continued to hold the collateral agreements and the securities pledged thereunder and at no time were these instruments transferred or assigned to Reconstruction Finance Corporation by express agreement. Although the indebtedness of C. M. Pearce to the Bank, other than the $230,000 loan, was twice reduced to $1.00, Pearce never made demand upon the Bank for return of the securities. . . .

". . .

"The primary and substantial question presented by this appeal is whether the terms of the

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this Note shall mean any funds, guarantees, or other property or rights therein of any nature whatsoever or the proceeds thereof which may have been, are, or hereafter may be, hypothecated directly or indirectly, by the undersigned or others, in connection with, or as security for, the Indebtedness, or any part thereof. The Collateral, and each part thereof, shall secure the Indebtedness, and each part thereof.' "

[2] "12. Sharing of Collateral. Any and all security or guaranty of any nature, including but not limited to rights of setoff and counterclaim, which Bank or RFC may at any time receive or have, jointly or severally, to secure Bank or RFC with respect to any such loan shall secure the interests of Bank and RFC therein in the same proportion as such interests bear respectively to the entire unpaid balance of the loan."

collateral agreements, as above described, and the subsequent transactions between the parties, subjected the collateral pledged thereby to foreclosure for payment of the unpaid balance due on the $230,000 note. It is not suggested that there is any illegality in the provisions of the collateral agreement which include unspecified future obligations of C. M. Pearce. The claim is that the collateral securities were not subject to the indebtedness because they should be construed to secure only the indebtedness of C. M. Pearce individually, and that even this was not accomplished in the present case because there was never any express assignment made by the Bank to Reconstruction Finance Corporation, nor did it ever have possession of the securities or claim to have a lien thereon until the filing of the second amended complaint in this case. It is further vigorously asserted by the appellants that the pledgors were in no wise bound by the terms of the 'participation agreement' quoted above. It is not contended, however, that C. M. Pearce is not liable for payment of the note in question. It [is] evidenced at least a second liability upon his part to the Bank within the provisions of the collateral agreement. These we have already set forth in full and from them it is clear that as between Pearce and the Bank the collateral represented security for the obligation. The assignment of this note by the Bank to Reconstruction Finance Corporation with a retention of 25% interest therein did not operate to release the collateral, since the agreements specifically provided that the instrument, rights and powers granted thereunder and securities pledged, could be transferred and assigned at such time and upon such terms as the Bank might deem advisable. When such obligation was transferred and assigned, the assignee became also entitled to the claim of lien possessed by the Bank. None of the asserted agreements between the other pledgors and Pearce are even claimed to have been brought

to the attention of the Bank prior to the time the loan in question was made. The rights of the parties must be determined by the terms of the collateral agreement and the instruments which Pearce executed. The facts of the case support the finding of the trial Judge that the collateral in question was subject to the obligation of the note and that Pearce and the Bank had so considered and treated it. Under these circumstances it is not legally material that Reconstruction Finance Corporation, for a time, was ignorant that the Bank held such collateral, and that it stated to Rucker and McGee that it did not so have it. Neither of the parties acted upon such statement, or were in any way prejudiced thereby. The right to this security arose by operation of law and the facts of the case under the terms of the collateral agreements, and upon the discovery of their existence this right could be enforced in this proceeding by the joint owners of the obligation which the collateral secured. The Court did not err in adjudging this claim superior to those of the appellants who held assignments expressly subject to the claim of the Bank, and in further adjudging that this claim was effective upon the security pledged by Mrs. Pearce and Atkinson."

The issue is whether the $230,000 loan was a loan of Reconstruction Finance Corporation and the Mercantile National Bank at Dallas or an exclusive loan of the Bank. Petitioners claim it was a Reconstruction Finance Corporation and Mercantile Bank loan and as such loan it was not covered by the pledge contracts whose terms limit the subjection of the capital stock pledged to debts due or to become due to the original pledgee, the Bank. Respondents claim that the loan was an exclusive loan of the Bank and is covered by the terms of the pledge contracts.

Jurisdiction

The jurisdiction of this Court is invoked under the Judicial Code (28 U.S.C. 1254(1)). The Court of Appeals denied petition for rehearing on June 18, 1952.

Questions Presented

1. Did the Court of Appeals err in failing to hold that the collateral agreements executed by petitioners herein limited the subjection of their collateral to debts due or that became due in favor of the Mercantile National Bank at Dallas—original pledgee?

2. Did the Court of Appeals err in affirming the judgment for respondents that the collateral (of petitioners) was subject to the obligation of the note sued on?

3. Did the Court of Appeals err in holding that the right to this security arose by operation of law and the facts of the case under the terms of the collateral agreements?

4. Did the Court of Appeals err, as a matter of law, in failing to strictly construe the contracts of pledge?

5. Did the Court of Appeals err, as a matter of law, in failing to construe the contracts of pledge in the light of the circumstances existing at the time of their execution?

6. Did the Court of Appeals follow and apply the Texas law in holding that the contracts of pledge executed by petitioners secured the Reconstruction Finance Corporation?

Reasons for Allowance of the Writ

The decision below is in conflict with applicable decisions of this Court, and also with other decisions

of the court below and other courts of appeal on the same matter.

(1) The holding that petitioners' Travelers Insurance Company stock was subject to a debt due Reconstruction Finance Corporation and the Bank is in conflict with *George D. Harter Bank of Canton, Ohio v. Inglis,* 6 Cir., 6 F. 2d 841 (1925, cert. den. 269 U.S. 576). In the Harter case the Court of Appeals held that the contract of pledge there considered limits the subjection of the collateral to debts due or to become due to the original pledgee, City National Bank. To the same effect have been the later decisions of, *In Re: Haynesworth, et al.,* 34 F. 2d 334, *Jones v. Kendall,* (1929) 4 Cir., 34 F. 2d 344, *Union Trust Co. v. Pocahontas Sp. School District,* 189 Ark. 1019, 76 S.W. 2d 60 (1934), 72 C.J.S. 79, §44, 21 R.C.L. 673, *Pollak v. Kahn,* 17 F. Supp. 750.

(2) Petitioners are entitled as a matter of law to a strict construction of the pledge contracts executed, where the Bank insists that the lien there created covers a debt due some one other than the original payee. *Gillett v. Bank of America,* 160 N.Y. 549, 55 N.E. 292 (1899); *Holston National Bank v. Wood,* 125 Tenn. 6, 140 S.W. 31 (1911); *St. Lucie County Bank & Trust Co. v. Aylin,* 114 So. 438; *Heffner v. First National Bank of Huntington,* 311 Pa. 29, 166 A. 370, 87 A.L.R. 610; 72 C.J.S. 42, §28(1).

(3) Petitioners are entitled as a matter of law to a construction of the pledge contracts in the light of the circumstances existing at the time of their execution. There is no dispute here as to what the parties did, or what words they used. The question is what was the meaning and intention of the parties? What was their agreement? *Scott v. United States,* 12 Wall 443, 20 L.

Ed. 438; *Reed v. The Merchants' Mutual Insurance Company of Baltimore,* 95 U.S. 23, 24 L. Ed. 348; *Sand Filtration Corporation v. Cowardin,* 213 U.S. 360, 29 S. Ct. 509, 53 L. Ed. 833; *Lockwood v. Ohio River Railway Co., et al.,* 103 F. 243; *West v. Commissioner of Internal Revenue,* 5 Cir., 150 F. 2d 723; *West, et al., v. Continental Oil Co.,* 5 Cir., 194 F. 2d 869; *Atterbury v. Bank of Washington Heights,* 241 N.Y. 231, 149 N.E. 841; *Moran v. Standard Oil Co.,* 105 N.E. 217, 211 N.Y. 187; 49 C.J. 920.

Conclusion

Wherefore, petitioners pray that this Court issue a writ of certiorari, directed to the United States Court of Appeals for the Fifth Circuit, and that the judgment of the Court of Appeals and the judgment of the District Court be reversed by this Honorable Court.

MRS. KATE H. PEARCE,
CHARLES P. ATKINSON,
Petitioners

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July, 1952

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

Opinions of the Courts Below

The opinion of the Court of Appeals is reported in 195 F. 2d 396. The District Court's oral opinion is in the record at pages 249, 250, 251.

Jurisdiction

The judgment complained of was entered by the Court of Appeals for the Fifth Circuit on March 22, 1952, and the petition for rehearing was overruled by that Court June 18, 1952. The jurisdiction of this Court is invoked under the Judicial Code. (28 U.S.C. 1254(1))

Statement of the Case and Questions Presented

For a statement of the case and the questions presented, see the foregoing petition. (p. 2, et seq.)

Specification of Errors

1. The Court of Appeals erred in failing to hold that the collateral agreements executed by petitioners herein limited the subjection of their collateral to debts due or that became due in favor of the Mercantile National Bank, original pledgee.

2. The Court of Appeals erred in affirming the judgment for respondents that the collateral (of petitioners) was subject to the obligation of the note sued on.

3. The Court of Appeals erred in holding that the right to this security arose by operation of law and the facts of the case under the terms of the collateral agreements.

4. The Court of Appeals erred, as a matter of law, in failing to strictly construe the contracts of pledge.

5. The Court of Appeals erred, as a matter of law, in failing to construe the contracts of pledge in the light of the circumstances existing at the time of their execution.

6. The Court of Appeals erred in holding, contrary to the Texas decisions, that the contracts of pledge executed by petitioners secured the Reconstruction Finance Corporation and Bank.

Argument

After study of the opinion of the Court of Appeals we believe that the Court had overlooked the fact that the contracts of pledge executed herein limited the subjection of the collateral to debts due or to become due to the original pledgee. We emphasized this point in our motion for rehearing. The issue of whether the $230,000 loan was a loan of Reconstruction Finance Corporation and the Mercantile National Bank or an exclusive loan of the Bank became crystallized when the Court denied our motion for a rehearing. For the Court's holding that the right to this security arose by operation of law was in effect a holding that the loan in question was an exclusive loan of the Bank. (Op. 9)

In its opinion the Court did not say in so many words that the $230,000 loan was an exclusive loan of the Bank, but it could not have reasoned otherwise for without such a finding the right to the security could not have arisen by operation of law.

We agree that the pledgee's transfer of a secured debt carries with it a transfer of the collateral, notwithstanding the collateral is not actually delivered to the transferee. It is petitioners' contention that the $230,000 note assigned was not secured by the lien that

we created and that assignees of the note cannot look to such lien which was not in anyway incident to the note.

The participation agreement executed by Reconstruction Finance Corporation and Mercantile National Bank on April 14, 1945, provided to whom a participation loan could be made. It provided for the maximum amount said loan could be made for. It provided for the interest rates to be charged and for the possession of notes and collateral incident to the loan. (R. 145, 146) With this premise that the loan was a loan of Reconstruction Finance Corporation and the Bank we respectfully submit the following:

The collateral agreements which were executed by petitioners Kate H. Pearce and Charles P. Atkinson were the only agreements entered into between the Bank and these guarantors. To paraphrase, the contract by which the guarantors became bound was voluntary on their part without profit or advantage, and without having in view the prospect of gain. It was an act of benevolence to the obligor and convenience to the obligee, and of emphatic use to both.

The Court of Appeals has said, "The rights of the parties must be determined by the terms of the collateral agreement and the instruments which Pearce executed." (Op. 8)

We agree that our rights must be determined by the terms of the collateral agreement. We cannot agree that we are to be affected in any way by other instruments C. M. Pearce executed. We urge this Court to examine the separate collateral agreements that we executed. (R. 90, 91) These contracts of pledge limit the subjection of the collateral to debts due or to become

due to the original pledgee, the Bank. There is no provision in these identical separate collateral agreements that we were to secure all debts to the holder or holders, and therefore a holding that Reconstruction Finance Corporation likewise may thus broadly use the security under the terms of these agreements is not a correct judgment. We did not create a power, or agency, to pass over the security for the broad purpose of securing any holders other than the Bank. True, the collateral agreements do provide that the instruments, rights and powers granted thereunder and securities pledged, could be transferred and assigned, but the effect of such assignment would have been to stand the assignee in "the shoes of Bank" as to the debt due the Bank before assignment.

This probably explains the Bank's failure to make an express assignment of the debt and the collateral agreements, and its resort to the device of the dollar note as a means to hold the property of petitioners herein. Had the Bank indorsed the dollar note to Reconstruction Finance Corporation the only debt that could have been secured under the terms of the collateral agreement was the dollar note.

The collateral agreements executed by petitioners herein simply lacked adequate terms of appropriation to secure the Reconstruction Finance Corporation and the Bank.

In the case of *George D. Harter v. Inglis,* 6 F. 2d 841 (1925, cert. den.) the Court in distinguishing contracts of pledge which provide security for "holder or holders" from pledge agreements which provide that the only holder shall be payee, stated at page 841:

> "Counsel for the bank rely on Mulert v. National Bank of Tarentum, 210 F. 857, 127 C.C.A.

419; Richardson v. Winnisimmett, 189 Mass. 25, 75 N.E. 97; Oleon v. Rosenbloom, 247 Pa. 250, 93 A. 473. None of them is in point. They deal with contracts of pledge subjecting the collateral, not merely to debts due the original pledgee, but to all debts and liabilities due any holder of the note, and authorizing any such holder to sell the collateral and apply the proceeds in payment of any debt then due or to become due, or that might thereafter be contracted in favor of any holder of the note. The contract of pledge in the instant case limited the subjection of the collateral to debts due or to become due or that thereafter might be contracted in favor of the original pledgee. . . ."

To the same effect have been the later decisions of *In Re Haynesworth, et al.,* 34 F. 2d 334, and *Jones v. Kendall,* 34 F. 2d 344 (1929) 4 Cir., affirming the District Court on the material issue.

In Union Trust Co. v. Pocahontas Sp. School District, 189 Ark. 1019, 76 S.W. 2d 60, (1934) the Arkansas Supreme Court said, at page 63:

> "But the note given by the Randolph State Bank pledges the collateral security for the payment of this note or any other liability of the said undersigned to the Bankers' Trust Company. It does not say 'or the holder.' Therefore there is no authority in this note to give the assignee, as holder, a right to apply the collections from this collateral to any other indebtedness. It is true that the clause giving a right to sell the collateral uses the word 'holder,' but there is no authority in the note for the payment to any holder except the Bankers' Trust Company."

See also 72 C.J.S. 79, §44, 21 R.C.L. 673, *Pollak v. Kahn,* 17 F. Supp. 750.

Petitioners are entitled to a strict construction of the pledge contracts executed.

Especially is this true here, where respondents are contending that the $230,000 obligation is secured under the terms of the pledge contracts executed.

In the case of *Holston National Bank v. Wood,* 140 S.W. 31, (Tenn. Sup. 1911) it was held at page 34:

> "While it has been held in Tennessee (Hanover National Bank v. Brown, 53 S.W. 206) that these provisions in a note authorizing a bank to hold as security for a general indebtedness that property pledged for a particular debt are valid, nevertheless an examination of the authorities shows the rule to be that such an agreement will not be construed so as to extend the obligation beyond that intended by the pledgor; and, if such agreement is on a printed form furnished by the bank and signed by its customer, and any doubt arises as to its proper interpretation, it will be construed in favor of the customer. Harris v. Frankfort Bank, 77 Md. 423, 26 Atl. 523; Hathaway v. Fall River National Bank, 131 Mass. 14; . . ."

In *Gillett v. Bank of America,* 160 N.Y. 549, 55 N.E. 292 (Court of Appeals of N.Y., 1899) the Court said at page 294:

> "The reason for the rule that the language of an instrument is to be construed against the person who proposes it, rather than against the person who is invited to accept it, is that men are supposed to take care of themselves, and that he who chooses the words by which a right is given ought to be held to the strict interpretation of them rather than he who only accepts them. . . ."

In *Heffner v. First Nat. Bank of Huntingdon, Pa.,* 166 A. 370, 87 A.L.R. 610 (Pa. Sup. 1933) the Court in construing a pledge agreement said, at page 372:

> "A pledge, like any other contract, where there is any doubt as to its meaning must be construed

with some degree of strictness against the party preparing it. Kelter, Tr., v. American Bankers' Finance Co., 306 Pa. 483, 160 A. 127; National Bank of Kentucky v. Gallagher, 243 Ky. 740, 49 S.W. 2d 1006, . . . The form signed by appellant and her husband was the usual printed form note of appellee, and it was for the bank that prepared it to word it clearly in accordance with the meaning it now insists upon, by inserting words which adequately conveyed that meaning."

In *St. Lucie County Bank & Trust Co. v. Aylin, et al.*, 114 So. 438, (Florida Sup. 1927) at page 440, the Court stated:

> "When this presumption is indulged in, (presumption that bank dictated the terms and conditions of the loans made) as it was evidently indulged in by the chancellor, then the rule that one of the parties to a contract, having chosen the language applied and being responsible for any alleged uncertainty and ambiguity, must suffer the result of having such language construed against him, may be invoked. That such is a sound and just rule has been held to be true by this court in L'Engle v. Overstreet, 61 Fla. 653, 55 So. 381; Brown v. Beckwith, 60 Fla. 310, 53 So. 542, . . ."

See also 72 Corpus Juris Secundum, page 42, §28(1).

There is abundant authority for the proposition that a court will construe the contract of pledge "according to the real intention of the parties" at the time of execution, which would logically involve a consideration of the circumstances attending the transaction from which such intention could be inferred.

In *Reed v. The Merchants' Mutual Insurance Company of Baltimore*, 95 U.S. 23, 33 (1877), this Court stated, at page 30:

> "Although a written agreement cannot be varied (by addition or subtraction) by proof of the circumstances out of which it grew and which surrounded its adoption, yet such circumstances are constantly resorted to for the purpose of ascertaining the subject matter and the standpoint of the parties in relation thereto. Without some knowledge derived from such evidence, it would be impossible to comprehend the meaning of an instrument, or the effect to be given to the words of which it is composed. This preliminary knowledge is as indispensable as that of the language in which the instrument is written. A reference to the actual condition of things at the time, as they appeared to the parties themselves, is often necessary to prevent the court, in construing their language, from falling into mistakes and even absurdities."

In *Charles G. Scott v. United States,* 20 L. Ed. 438, 439 (1871) this Court stated:

> "In cases like this it is the duty of the court to assume the standpoint occupied by the parties when the contract was made—to let in the light of the surrounding circumstances—to see as the parties saw, and to think as they must have thought, in assenting to the stipulations by which they are bound. This process is always effective."

In *Sand Filtration Corporation of America v. Cowardin,* 213 U.S. 360, 365 (1909) this Court said at page 364:

> "The object of construction is to effectuate the intention of the parties in making a given contract. When the contract is in writing the language used should be interpreted in the light of the circumstances surrounding the parties at the time the contract was made."

To the same effect have been other decisions of this

Court. *United States v. Peck,* 102 U.S. 64, 26 L. Ed. 46; *Merriam v. United States,* 107 U.S. 437, 27 L. Ed. 531; *United States v. Gibbons,* 109 U.S. 200, 27 L. Ed. 906. See also Wigmore, Evidence, 3rd Ed., §2470, page 227; 3 Williston, Contracts, Rev. Ed. 1780 (1936).

In *Lockwood v. Ohio River Railway Co., et al.,* 103 F. 243, 249 (1900) 4 Cir., the Court stated, at the top of page 246:

> ". . . it is always the duty of the court, in all cases where they are susceptible of different constructions, to take into consideration the circumstances attending the transaction, the particular situation of the parties, and the state of the thing granted, for the purpose of ascertaining the true intent; for the intention of the parties is manifestly paramount to the manner chosen to effect it. The courts therefore may avail themselves of the same light which the parties enjoyed when the contract was executed, and may place themselves in the same situation as the parties who made it, in order that they may view the circumstances as those parties viewed them, and so judge of the meaning of the words and the correct application of the language to the things described; and if any of the terms used seem to contradict the manifest intention, as clearly indicated by the agreement as a whole, the intention must govern."

In *West v. Commissioner of Internal Revenue,* 150 F. 2d 723, (1945) 5 Cir., the Court said:

> "In determining the character of the contract, we are dealing with a deed and a contemporaneous written agreement. We may look not only to the language employed in both instruments, but to the circumstances surrounding the parties when the instruments were executed."

In *West et al. v. Continental Oil Co.,* 194 F. 2d 869,

(1952) 5 Cir., it was held, on page 871, that a mineral lease must be construed in the light of circumstances existing at the time of its execution. Circuit Judge Rives goes on to say in his opinion that, "Apparently neither of the parties clearly foresaw the possibility that the price of oil might advance so as to make the continued operation of the existing well profitable, and at the time of the execution of the lease, nothing was said about the drilling of additional wells, etc."

Petitioners respectfully submit that at the time they executed the Bank's pledge contracts neither of the parties contemplated that the properties of petitioners herein would ever be looked to as security for anything other than C. M. Pearce's personal debt due the Mercantile National Bank.*

In *Perron v. First Nat. Bank,* 286 N.W. 859 (Mich. Sup. 1939) the Court, at page 860, says:

> "The determination of the legal effect of the pledge is controlled by the intention of the parties. If the contract of pledge prepared by the pledgee is not clear as to whether the collateral shall secure a particular indebtedness, it must be construed in favor of the pledgor; and when there is a provision in a pledge as to general indebtedness, the intention of the parties, especially the pledgor is the controlling element. . . ."

In *Fullerton v. Chatham National Bank,* 40 N.Y.S. 874, the Court in construing a general indebtedness provision in a pledge agreement said, on page 876:

> "But the decisive consideration in restricting the securities to the individual obligation of Judge Fullerton is the silence of the agreement as to the firm indebtedness. Had the intention been to cover

*See Appendix, p. 24.

that indebtedness, we may be sure it would not have been allowed to lurk in equivocal phraseology, but would have been declared in the explicit terms exacted by ordinary prudence, and habitual with bank officers. Bank officers are not wont to advance money upon an ambiguity."

See also *Torrance v. Third Nat. Bank,* 3 Cir., 210 F. 806, and *In Re Evans,* 3 Cir., 238 F. 543, 544.

In *Gillett v. Bank of America,* 55 N.E. 292, the Court said, at page 294:

> "In the construction of written contracts it is the duty of the court, as near as may be, to place itself in the situation of the parties, and from a consideration of the surrounding circumstances, the occasion, and apparent object of the parties, to determine the meaning and intent of the language employed. Indeed, the great object, and practically the only foundation, of rules for the construction of contracts, is to arrive at the intention of the parties. This is a most conspicuous and far-reaching rule, and involves the nature of the instrument, the condition of the parties, and the objects which they had in view; and, when the intent is thus ascertained, it is to be effectuated, unless forbidden by law."

The Court said at page 295:

> ". . . the fact that a construction contended for would make the contract unreasonable and place one of the parties at the mercy of the other may properly be taken into consideration. . . ."

The participation agreement between the bank and the Reconstruction Finance Corporation was executed on April 14, 1945. On this date the bank knew that seventy-five per cent of any joint loan made in accordance with such agreement was to be underwritten by Reconstruction Finance Corporation. If it had been

the bank's intention that the collateral agreements executed were to cover loans made by the Reconstruction Finance Corporation and the bank, it would have been declared in explicit terms. It was for the bank, which prepared the form, to word it in accordance with the meaning it now insists upon, by inserting words which adequately conveyed that meaning.

The Court quotes paragraph 12 of the participation agreement (Op. 5) relating to the "sharing of collateral" which provides that "all security or guaranty . . . shall secure the interests of bank and RFC therein in the same proportion as such interests bear respectively to the entire unpaid balance of the loan."

We call this Court's attention to paragraph 14 of the participation agreement, which we quote:

> "Possession of Notes and Collateral. Bank shall hold the note or notes evidencing each such loan, all the collateral therefor and all instruments delivered in connection therewith; provided, however, that at any time subsequent to the purchase by RFC of a participation in any such loan Bank shall, upon five days' written demand therefor by RFC, transfer to RFC without recourse, the note or notes, collateral and *all* instruments executed in connection with such loan, *all* of which shall thereafter be held by RFC and simultaneously therewith RFC shall issue to Bank a certificate of interest (on RFC Form L-303) evidencing the interest retained by Bank in such loan." (R. 146)

The certificate of interest was issued by Reconstruction Finance Corporation to the bank on February 13, 1947. Simultaneously with the issuance of this certificate of interest, the bank delivered to the Reconstruction Finance Corporation "all instruments executed in connection with such loan." The collateral agreements executed by appellants were not a part of

this delivery, and we submit that they should have been in order for the bank's position to be consistent.

The Texas Rule

In *San Antonio Nat. Bank v. Blocker,* 77 Tex. 73, 13 S. W. 961, the Texas Supreme Court in construing a general indebtedness provision held that collateral security cannot be appropriated as security for any debt or purpose other than that covered by the agreement of the parties.

The rule was restated and followed in the more recent Texas case of *LeLeux v. Serafino,* 88 S.W. 2d 1100.

Conclusion

Petitioners therefore pray that this Court grant the writ of certiorari herein prayed for, and that this Court reverse the judgment of the Court of Appeals and that of the District Court.

Respectfully submitted,

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Counsel for Petitioners

Charles P. Atkinson
Of Counsel

July, 1952

APPENDIX

Mr. Ben F. Read, a former Vice-president of the Bank, testified that he handled all of the transactions in connection with the making of loans to C. M. Pearce individually and Apex Drilling Company. (R. 86) Mr. Read related that the individual loans of the Bank to C. M. Pearce were secured by the properties delivered to the Bank with the two pledge agreements signed by C. M. Pearce, Jean E. Collins and petitioners Kate H. Pearce and Charles P. Atkinson. (R. 87, 88, 92)

Mr. Read testified on cross-evamination that

> ". . . we were never quite clear whether or not we could—because of these loans being made at separate times, and the collateral being put up at separate times—whether or not we could retain the collateral to apply on the portion that the bank would be carrying on the big loan." (R. 107)

Mr. Fred B. Cable, examiner in the Dallas office of the R.F.C., testified in answer to questions asked on cross-examination that the Union Bank and Trust Company stock was not a part of the collateral to the Apex Drilling Company, Inc., loan. (R. 136, 137, 138) Both Union Bank and Trust Company stock and Travelers stock were pledged and described in the same contracts of pledge; if the Union Bank stock was not collateral to the loan, the Travelers stock could not be a part of the security either. Mr. Cable acknowledged too that he had written a letter to Mr. McGee on April 5, 1950, in which he advised that the stock in question was being held by the Bank in connection with a personal loan of the Bank to C. M. Pearce, and that this can be verified by Mr. Rankin, Vice-President of the Bank. (R. 136)

Mr. Rankin testified that Mr. Cable misunderstood

him. The following testimony of Mr. Rankin appears in the record: (R. 170-171)

"Q. Did you get a copy of the letter Mr. Cable wrote me under date of April 5, 1950?

"A. No, sir. I don't know anything about it.

"Q. He says, 'Receipt is acknowledged of your letter dated April 4, 1950, with reference to 20 shares of the capital stock of Union Trust Company of Fort Worth, which you say C. M. Pearce executed an assignment to you. This stock is not part of the collateral of the Apex Drilling Company loan now in liquidation.

" 'Upon inquiry, we have been advised by Mr. Rankin of the Mercantile National Bank in Dallas, that the stock is being held in connection with a personal loan of Mr. Pearce with the bank'?

"A. I told him it was covered under a collateral agreement with the loan at the bank.

"Q. You didn't tell him it was held in connection with a personal loan?

"A. No, sir, he misunderstood what I said.

"Q. Now then, you had a letter from me dated April 6, 1950, didn't you?

"A. Yes, sir.

"Q. In which, after some details, I told you that on April 4th I wrote you in respect to the matter, I wrote the RFC and sent you a copy of the communication, 'I am in receipt of a letter from Fred B. Cable, examiner for the RFC, in which he states this stock is not a part of the collateral held by the RFC, and upon inquiry he has been advised by you that the stock is held by your bank in connection with a per-

sonal loan of Mr. Pearce's. I am assuming that this statement is correct.'

"Then, I tell you I would be glad to send you a photostatic copy.

"Now, you never did deny that?

"A. No, sir."

Mr. Rankin testified further on redirect examination that the R.F.C. was notified of the "existence of this collateral" of appellants herein by one of the Bank Attorneys, Mr. Wiley Johnson. (R. 173)

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In the Supreme Court of the United States

OCTOBER TERM, 1952

No. 231

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RECONSTRUCTION FINANCE CORPORATION AND MERCANTILE NATIONAL BANK AT DALLAS, *Intervenor*

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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BRIEF IN OPPOSITION FOR THE RESPONDENT RECONSTRUCTION FINANCE CORPORATION

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JURISDICTION

The judgment of the Court of Appeals was entered on March 22, 1952 (R. 334-335). A petition for rehearing filed by petitioners April 12, 1952 (R. 337-344) was denied on June 18, 1952 (R. 345). The petition for a writ of certiorari was filed July 28, 1952. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether the assignment to the Reconstruction Finance Corporation of a secured note payable to a bank, pursuant to a preexisting arrangement for the Corporation to purchase on demand of the bank an interest in particular loans, gave the Corporation the benefit of collateral securing loans by the bank to the maker of the note.

STATEMENT

In May and June 1945, to induce the Mercantile National Bank at Dallas (hereinafter called the Bank) to lend money to C. M. Pearce, the petitioners[1] deposited shares of stock with the Bank as collateral security. The collateral agreements provided that the property pledged "may be held by said Bank as security for any and all debts and

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[1] Despite the caption, Kate H. Pearce, Pearce's mother (R. 41, 83) and Charles P. Atkinson, his nephew (R. 42, 83) are the only two petitioners (Pet. p. 1). Their positions and contentions are different from those of Mark McGee and R. H. Rucker, who were also appellants below.

obligations * * * to said Bank for the payment of money, whether such debts, liabilities and obligations now exist, or are hereafter incurred or arise", and also that all rights and powers thereunder "together with the securities then held in pledge hereunder, may be transferred and assigned by said Bank at such time and upon such terms as it may deem advisable; and such assignee shall succeed to all rights and powers of said Bank hereunder." (R. 90-91).

C. M. Pearce obtained several loans from the Bank. On September 15, 1945, he borrowed $200,000.00 on a note signed by him, d/b/a Apex Drilling Co. (R. 36). On March 26, 1946 the company was incorporated and a new loan, in the amount of $230,000.00, evidenced by a note dated March 26, 1946, payable to the Bank and signed by C. M. Pearce individually and as President of the firm, was given (R. 117). The proceeds satisfied the $200,000.00 note (R. 37). Subsequently, on February 5, 1947, the Bank assigned the note to the R.F.C. without recourse (R. 117). R.F.C. issued a certificate of interest dated February 13, 1947, certifying that the Bank reserved an equitable interest of twenty-five per cent of the loan (R. 147). The assignment to R.F.C. was in accordance with a participation agreement between R.F.C. and the Bank dated April 14, 1945.[2] (R. 145-146).

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[2] Under the "Blanket Participation Agreement" (R. 145-146) between R.F.C. and the Bank, R.F.C. was not a

On Pearce's failure to pay, R.F.C. sued for itself and the Bank to foreclose liens against the collateral securing the loans, joining petitioners as persons claiming an interest therein (R. 1-12). Petitioners answered, admitting that the collateral was pledged to the Bank under agreements to secure C. M. Pearce's personal indebtedness but denying the collateral was subject to the $230,000.00 indebtedness (R. 261-267). The Bank intervened and adopted the R.F.C.'s pleadings (R. 38, 267, 309-310). At the close of the evidence, the trial court entered judgment for plaintiffs (R. 268-276). In an oral opinion it held that the collateral was subject to the balance due to the R.F.C. on the original loan (R. 249-251). On appeal the Court of Appeals affirmed (R. 327-334). A petition for rehearing presenting the same question as the petition for certiorari was denied (R. 345).

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party to the loans and did not automatically acquire an interest therein, but the Bank might require it to purchase an interest (Par. 3, R. 145). "Upon ten days' written demand by Bank, R.F.C. will, at any time but not later than sixty days after maturity of the note * * * purchase for cash from Bank a participation of the Designated Percentage [not exceeding 75%]." For the right to call upon R.F.C. to purchase a participation the Bank paid a charge of three-fourths of one per cent per annum of the Designated Percentage of the unpaid principal balances of the loans. This corresponded to a premium for credit insurance. The loan to Pearce was close to the maximum in which R.F.C. agreed to participate.

ARGUMENT

As petitioners acknowledge, the issue is factual, "whether the $230,000 loan was a loan of Reconstruction Finance Corporation and the Mercantile National Bank at Dallas, or an exclusive loan of the Bank. Petitioners claim it was a Reconstruction Finance Corporation and Mercantile Bank loan and as such loan it was not covered by the pledge contracts * * *." (Pet. 7). Petitioners do not controvert the facts stated by the court below but adopt them.

The questions of pledge construction raised in the petition are purely hypothetical. Assuming that this Court will review the facts, petitioners assert that the R.F.C., although it was not a party to the Bank's 1946 loan to Pearce and acquired an interest only by virtue of the assignment dated February 5, 1947, was nevertheless an original lender, along with the Bank (Pet. 7), by reason of its April 14, 1945 commitment to purchase a share of the loan on demand (R. 145). But the two premises are wrong—the R.F.C. was not a lender, and petitioners have misunderstood the "*Blanket Participation Agreement* (For Deferred Participation by R.F.C. in Qualified Loans Made by Bank)".

The parties to a contract are ascertained by inspection of the documents. *United States* v. *Algoma Lumber Co.*, 305 U.S. 415, 421, 422; *Farm Security Administration* v. *Herren*, 165 F. 2d 554,

562 (C.A. 8), certiorari denied, 333 U.S. 875. The Bank negotiated the loan, made the 1946 loan commitment and loan, and was the payee of the note (R. 117). The proceeds went to pay loans by the Bank. The Bank was under no obligation to sell a share of the loan to R.F.C. It merely had a "put" or underwriting commitment from R.F.C., whereby it might require R.F.C. to purchase a participation to supplement, not substitute for, its security.[3] Nowhere do petitioners directly allege that the R.F.C. acquired an immediate interest in the loan when it was made or at any time prior to February 5, 1947. The courts below implicitly decided that the loan to C. M. Pearce was not made by anyone but the Bank. The contention that the R.F.C. was a party to the loan seems to have been somewhat of an afterthought distinctly presented for the first time in the petition for rehearing in the Court of Appeals (Pet. 12).

The alleged conflict with *George D. Harter Bank* v. *Inglis,* 6 F. 2d 841 (C.A. 6), certiorari

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[3] See Pars. 3(c), conditioning the Bank's power to require purchase on its not having made any disbursements on account of a loan "unless such loan was secured by validly pledged collateral having an appraised value * * * in excess of the unpaid balance of amounts previously disbursed on account of such loan and the amount then to be disbursed", and 12 of the Blanket Participation Agreement, providing that R.F.C. and the Bank would share collateral in the ratio of their interests in the loan (R. 145-6). Cf. *District of Columbia* v. *Hamilton Nat. Bank,* 76 Atl. 2d 60, 63 (Mun. Ct. App.).

denied, 269 U.S. 576, and petitioners' other citations, is non-existent, stemming from the fallacious assumptions that the R.F.C. was one of the lenders and that R.F.C. is improperly seeking to hold collateral pledged solely to secure indebtedness to the Bank. The Harter Bank, after absorbing City National Bank in 1922, sought to apply on its own loan to Geiger-Jones collateral which had been deposited with City National to secure loans made by that bank. The question was whether the collateral Geiger-Jones deposited with City National might, "after the existing debt is paid, be applied to the payment of a pre-existing obligation to another bank which has absorbed the bank with which the collateral was deposited." 6 F. 2d, at 843. The court held that as against Geiger-Jones' receiver the collateral *was* available to the Harter Bank only for the debt arising out of the City National loan, and that the surplus could not be applied to the separate debt originally owed the Harter Bank. *In re Haynsworth,* 34 F. 2d 334, 336 (E.D. S.C.), modified 34 F. 2d 344 (C.A. 4) is almost identical with the *Harter Bank* case in denying that the collateral was liable for *independent* demands of the assignee.

The decision below is manifestly correct. Petitioners specifically consented to an assignment of the collateral and agreed that any assignee would succeed to all rights and powers of the Bank with

respect to the collateral. In derogating from their consent to assignment and from the consequences that would flow from depositing collateral to secure the existing and future indebtedness of Pearce to the Bank in the absence of a specific agreement,[4] petitioners seek to release their collateral from the lien to which they subjected it after loans had been made in reliance on their collateral. Like any other party to an agreement, a pledgor is not to be held beyond his undertaking and he may make that as narrow as he likes, at the time the agreement is made. Cf. *Portuguese-American Bank* v. *Welles*, 242 U.S. 7, 11.[5] However, pledged collateral is bound when the pledgors have expressly agreed that any assignee should have all the rights of the lender. The specification as to assignment in the collateral agreement was inserted with a view to sale. Its inclusion must have enhanced the attractiveness of the loan to the Bank.[6] Without the agreement as to assignment of collateral the Bank might not have made the loan to Pearce: the loan might have

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[4] *Hooper* v. *Robinson*, 98 U.S. 528, 539; *Plitt* v. *Stonebraker*, 195 F. 2d 39, 42 (D. D.C.); *District of Columbia* v. *Hamilton Nat. Bank*, 76 Atl. 2d 60, 64; A.L.I., Restatement of Contracts, § 171(2).

[5] After advances have been made the collateral cannot be withdrawn. Cf. *United States ex rel. Wilhelm* v. *Chain*, 300 U.S. 31, 34.

[6] The agreement with R.F.C. of April 14, 1945, is concrete proof that the possibility of sale was envisaged.

been risky or undersecured; prospective assignees might have been troubled by the absence of an assignment clause; and without R.F.C. as a prospective assignee the loan might have been too large for the Bank. It is idle to say that the petitioners were guarantors who did not have the prospect of gain (Pet. 13). Their collateral agreements were intended to induce the Bank to make a loan. The Bank would benefit from the assurance that any assignee would succeed to all its rights, since availability of the security to assignees would be reflected in the amount that could be realized on a sale of an interest in the note, whether to the R.F.C. or another. For petitioners to argue that the collateral did not remain security in the hands of the R.F.C. as assignee is to defeat their own solemn engagement that the collateral would be available on the occurrence of the contingency it was designed to cover, a default by C. M. Pearce which would cause the Bank or its assignee to look to the collateral.

Petitioners were in no way prejudiced or aggrieved by the assignment to R.F.C. The participation agreement of 1945 may well have made possible the loans to C. M. Pearce, which is what the posting of collateral was designed to accomplish. It should have been a matter of indifference to petitioners who held the note. So long as the burden on the collateral was not enlarged, it was *res inter alios acta.* The fact that

the assignment was effected under a general agreement between the Bank and R.F.C. did not make the latter a party to the loan. The 1945 agreement confirms the foreseeability of assignment and the importance to the Bank of full assignability. But under that agreement R.F.C. obtained no participation in the loan when it was made or at any time until 1947, when the Bank called upon it to purchase an interest. The petitioners gain nothing by argumentative assertions that the collateral would be unavailable to secure original loans made by R.F.C., either alone or jointly with the Bank, when such loans are not in issue.

Since the separate collateral agreements included no exceptions for subsequent assignments pursuant to a general arrangement between the Bank and R.F.C. for purchase of a participation on demand, none may be interpolated into the agreement. Cf. *Harrison* v. *Fortlage,* 161 U.S. 57, 63; *Dermott* v. *Jones,* 2 Wall. 1, 8; *Guttmann* v. *Illinois Central R. Co.,* 189 F. 2d 927, 930 (C.A. 2), certiorari denied, 342 U.S. 867. The courts do not "disregard words used by the parties, descriptive of the subject matter, or of any material incident, or to insert words which the parties have not made use of." *Harrison* v. *Fortlage,* 161 U.S. 57, 63; *Chicago R.I. & P. Ry. Co.* v. *Maryland Casualty Co.,* 75 F. 2d 596, 599 (C.A. 8). The agreement should be enforced. Cf. *Twin City Co* v. *Harding Glass Co.,* 283 U.S. 353, 356.

Petitioners seek a windfall defeasance of their pledge from the circumstance that the Bank entered into the forehanded arrangement with R.F.C., with the Bank paying for the right to require R.F.C. to purchase part of the loan. Their claim that the collateral was released from liability for C. M. Pearce's debts on loans by the Bank as soon as R.F.C. purchased a participation is without merit.

CONCLUSION

It is respectfully submitted that the petition for a writ of certiorari should be denied.

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